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No. 96-235

In The

Supreme Court of the United States

October Term, 1995

FRANCHISE TAX BOARD OF
THE STATE OF CALIFORNIA,

Petitioner,

v.

STEPHEN B. MACFARLANE,

Respondent.

**On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit**

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

If the allocation of burden of proof in litigation of bankruptcy tax claims is important, why did the only two circuits who have addressed the issue since 1898 have to resort to dicta to decide it?

Should this Court review the judgment of the Ninth Circuit Court of Appeals for the question posed by Petitioner even though the judgment should be affirmed because:

(a) Petitioner presented no evidence and therefore affirmance of summary judgment is proper; and

(b) The claim of the Petitioner was not entitled to presumptive validity because it was based solely on an IRS report which was withdrawn by the United States Department of Justice; and

(c) The claim of the petitioner was not entitled to presumptive validity because assessment was barred by 11 U.S.C. § 362(a); and

(d) All Circuits are unanimous that a claimant asserting a claim for taxes incurred after commencement of a bankruptcy case has the burden of proving all elements of its claim; and

(e) It is well settled that any claim in bankruptcy is entitled only to rebuttable presumption validity under F.R.B.P. 3001(f); and

(f) Any result other than the result in the Ninth Circuit would result in potentially at least 53 different burdens of proof applicable in determining tax claims in bankruptcy cases contrary to the uniformity intended by,

QUESTIONS PRESENTED – Continued

among other provisions, 11 U.S.C. §§ 346, 505, 728, 1146 and F.R.B.P. 3001(f); and

(g) The burden of proof rule in a controversy between a tax claimant and a taxpayer is not applicable to the controversy in a bankruptcy case between the tax claimant and other claimants who seek to share the taxpayer's estate; and

(h) The question asserted by Petitioner is not raised by the facts; and

(i) The decisions claimed to be in conflict are not in conflict because one dealt with a federal tax claim and the case at hand deals with a state tax claim in which issues of uniformity are more germane.

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OPINIONS BELOW

Respondent adopts the Petitioner's Statement of Opinions Below.

JURISDICTION

Respondent adopts the Petitioner's Statement of Jurisdiction.

CONSTITUTIONAL PROVISIONS, STATUTES AND RULES INVOLVED

Respondent adopts the Petitioner's Statement of Constitutional Provisions, Statutes and Rules Involved noting that although F.R.B.P. Rule 3001(f) is referenced in Petitioner's Statement, it is not included in Petitioner's Appendix as Petitioner represents at page 2 of its brief. Rule 3001(f) states:

> (f) **Evidentiary Effect.** A proof of claim executed and filed in accordance with these rules shall constitute prima facie evidence of the validity and amount of the claim.

Respondent suggests that the following statutes are also relevant:

11 U.S.C. § 346
11 U.S.C. § 362(a)
11 U.S.C. § 507(a)(8)
11 U.S.C. § 728
11 U.S.C. § 1107(a)
11 U.S.C. § 1146

STATEMENT OF THE CASE

Respondent commenced his bankruptcy case in 1990. The Internal Revenue Service subsequently asserted a claim for income taxes based on an audit report it issued on June 25, 1991. Respondent objected to this claim and the United States Department of Justice accepted as settlement a minor portion of the amount claimed.

Petitioner asserted a claim on April 3, 1992 based solely on the Internal Revenue Service report abandoned by the United States Department of Justice. Respondent objected to Petitioner's claim and filed depositions and declarations of witnesses and 849 pages of documentary evidence. Petitioner submitted no evidence. Respondent also contended that the issue of who has the burden of proof was irrelevant because inasmuch as no assessment had been made because it was barred by 11 U.S.C. § 362(a)[1] and the claim was based solely on an IRS report which had been withdrawn, no state presumption of validity arose and also because no controverted fact was in issue.

Respondent contended that the language in *IRS v. Levy (In re Landbank Equity Corp.)*, 973 F.2d 265 (4th Cir. 1992) (hereafter "*Levy*") was dicta and irrelevant because in that decision no evidence was presented to rebut the tax claim and accordingly the decision was proper under

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[1] **362. Automatic stay**

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title . . . operates as a stay. . . .

F.R.B.P. 3001(f) without application of any other burden of proof rule.

The facts to be reviewed are not those with which Petitioner takes considerable license in its statement but rather those found at pages 37 through 42 of Petitioner's Appendix as determined by the bankruptcy court. These facts were found by the Ninth Circuit to be uncontroverted and sufficient under applicable law to support judgment in favor of Respondent. Petitioner's Appendix at 11.

The Petitioner filed a notice of appeal, and the matter was ultimately heard by the district court. On June 29, 1994, the district court entered its judgment and memorandum decision affirming the bankruptcy court's denial of the state's proof of claim and reversing the bankruptcy court's summary determination, holding that genuine issues of material fact existed. Respondent filed a motion for reconsideration of this self-contradictory decision which was denied.

The Petitioner timely appealed to the United States Court of Appeals for the Ninth Circuit and the Respondent filed a cross-appeal. The matter was argued on March 6, 1996. That decision affirmed the holding of the district court which denied the Petitioner's proof of claim and reversed the holding of the district court which had held that genuine issues of material fact existed and remanded to the bankruptcy court for entry of judgment for Respondent on all issues. To obtain a review of that decision the Petitioner has filed its petition with this Court.

REASONS FOR NOT GRANTING THE WRIT

NEITHER THE NINTH CIRCUIT NOR THE FOURTH CIRCUIT HAD TO DECIDE WHO HAD THE BURDEN OF PROOF

In *Levy* the bankruptcy estate presented no evidence. Under F.R.B.P. Rule 3001(f) the claimant therefore wins. That was all that was required.

In the case at hand the estate presented almost a thousand pages of documents and depositions and declarations. The decision to be reviewed found both that there was no controverted fact and that the facts necessary to support a determination of nonliability had been determined.

There is no conflict in decision, only in principle, perhaps due to a failure of advocacy in the Fourth Circuit.

Furthermore, *Levy* recognized that its decision may apply only to federal tax claims inasmuch as it distinguished *California State Board of Equalization v. Official Unsecured Creditors Comm. (In re Fidelity Holding Co., Ltd.)*, 837 F.2d 696, 698 (5th Cir. 1988), which held that as to California state tax claims the federal standard of F.R.B.P. Rule 3001(f) alone applied. Respondent's Appendix at 38.

THERE ARE GROUNDS FOR AFFIRMING THE JUDGMENT OF THE NINTH CIRCUIT INDEPENDENT OF ITS PRONOUNCEMENT ON BURDEN OF PROOF

A prevailing party may "defend its judgment on any ground properly raised below. . . . ", *Washington v. Yakima Indian Nation*, 439 U.S. 463, 476 n. 20, 99 S. Ct. 740, 749 n.

20, 58 L. Ed. 2d 740 (1979); *Dayton Board of Education v. Brinkman*, 433 U.S. 406, 419, 97 S. Ct. 2766, 53 L. Ed. 2d 851 (1977); *Blum v. Bacon*, 457 U.S. 132, 137 n. 5, 102 S. Ct. 2355, 2359 n. 5, 72 L. Ed. 2d 728 (1982); *United States v. New York Telephone Co.*, 434 U.S. 159, 166 n. 8, 98 S. Ct. 364, 369 n. 8, 54 L. Ed. 2d 376 (1977).

As noted at Respondent's Appendix 2-25, Respondent urged that there was no burden of proof issue raised by the record because:

(a) no fact was controverted;

(b) no presumptive validity arose because no assessment was made and the claim was based solely on an IRS audit report abandoned by the United States Department of Justice (Respondent's Appendix 25);

(c) the Petitioner never cited any applicable state standard for burden of proof which applied in the presence of such facts (Respondent's Appendix 24).

As this Court has held, "We do not grant a certiorari to review evidence. . . . " *United States v. Johnson*, 268 U.S. 220, 227, 45 S. Ct. 496, 497, 69 L. Ed. 925 (1925). Petitioner is asking this Court to determine that the burden of proof matters in a decision in which no fact is controverted and in which several independent grounds for affirmance exist. Respondent does not believe that the issue contended to exist is apropos.

THE ISSUE PRESENTED IS NOT ONE OF PRESSING IMPORTANCE

The two decisions contended by Petitioner to be in conflict are the only two on the issue since 1898 to reach the merits and only then when they did not have to.

Furthermore *Levy* ignores the clear historical treatment of claims in bankruptcy as chronicled by the Respondent in the Ninth Circuit.

As Respondent noted before the Ninth Circuit, the law on this issue has been clear for a long time:

> The FTB's ubiquitous citations to *Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 67 S. Ct. 237 (1946) in support of its position fail to quote the most relevant passage from the opinion: "In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state where it sits." *Id.* at 329 U.S. 162. It should also be noted that in addition to the substantive decisions regarding the paramount nature of federal law in bankruptcy cases, a strong argument can be made that the FTB in filing its claim consented to a federal burden of proof rule. *See also*, E. Martin, *Consent: The Constitutional Basis for Bankruptcy Judge Authority*, 19 Cal. Bankr. J. 1 (1991).

Respondent's Appendix at 29.

Ironically, in *American Dredging Co. v. Miller*, 510 U.S. 443, 114 S. Ct. 981, 988, 127 L.Ed. 2d 285 (1994), cited by Petitioner, this Court noted that the federal burden of proof rule in admiralty has preempted contrary state rules since before 1942. Admiralty and bankruptcy have often been noted to have comparable considerations of uniformity and purpose.

THE DECISION OF THE NINTH CIRCUIT WAS CORRECT, FAIR AND ANY OTHER ALTERNATIVE WOULD CREATE CHAOS

As argued in the Ninth Circuit, Respondent's Appendix 27-28, the burden of proof rule which applies between a taxpayer and a tax claimant does not apply when the controversy is between the tax claimant and other creditors of the taxpayer competing for a portion of the assets of the bankruptcy estate of the taxpayer. All should be similarly situated.

The invalidity of Petitioner's allegation that the burden should be placed on the estate because it has access to evidence is demonstrated by *Levy* in which the estate lost because the trustee of the estate could present no evidence to rebut the claim in issue. Respondent's Appendix 27-28. Petitioner's assertion that trustees in bankruptcy have greater access to information than a taxing agency when the trustees assume control over the chaotic affairs of a bankrupt is generally not a reality. This circumstance in *Levy* supports Respondent's position that burden of proof rules applicable outside of bankruptcy do not apply in bankruptcy because the parties in interest are different. In a bankruptcy case the other creditors, rather than the debtor, are the persons in interest in the claims allowance process. Either a trustee, or a debtor in possession acting as a trustee pursuant to 11 U.S.C. § 1107(a),[2] represents the other creditors in this

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[2] 1107. Rights, powers, and duties of debtor in possession

(a) [A] debtor in possession shall have all the rights . . . and powers, and shall perform all the functions and duties . . . of a trustee serving in a case under this chapter.

process. This Court has always looked to the real parties in interest in controversies. For instance, in *Guidry v. Sheet Metal Workers Pension Fund*, 493 U.S. 365, 110 S. Ct. 680, 107 L. Ed. 2d 782 (1990), this Court noted that "the malefactor often is not the only beneficiary of the pension" in precluding an equitable exception to ERISA prohibition of alienation of a pension plan account. This result was subsequently applied in a bankruptcy context in *Patterson v. Shumate*, 504 U.S. 753, 112 S. Ct. 2242, 119 L. Ed. 2d 519 (1992). This issue was raised in the Ninth Circuit. Respondent's Appendix 40-43.

Whenever the tax claimant was intended to have an advantage, as in priority of a claim once established, the Code has stated the advantage. 11 U.S.C. § 507(a)(8).[3] It

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[3] **507. Priorities**

(a) The following expenses and claims have priority in the following order:

. . .

(8) Eighth, allowed unsecured claims of governmental units, only to the extent that such claims are for – . . . .

(A) a tax on or measured by income. . . .

(B) a property tax assessed before the commencement of the case and last payable without penalty after one year before the date of the filing of the petition;

(C) a tax required to be collected or withheld and for which the debtor is liable in whatever capacity;

(D) an employment tax on a wage. . . .

(E) an excise tax on – . . . .

(F) a customs duty. . . .

(G) a penalty . . . for actual pecuniary loss.

is well established that the burden of proof in establishing nondischargeability of a tax is on the taxing agency. *Grogan v. Garner*, 498 U.S. 279, 111 S. Ct. 654, 112 L. Ed. 2d 755 (1991). Since it is clear that a tax claimant has the burden of proof as to both priority and nondischargeability, it would be inconsistent to hold that it should be treated any differently as to other merits of its claim.

The Bankruptcy Code was intended to provide for uniformity of state taxation determination in many ways, see, e.g., 11 U.S.C. §§ 346,[4] 505,[5] 728[6] and 1146[7] in order to provide for uniformity throughout the country. The rule argued by Petitioner could conceivably require tax claims to turn on 50 state standards and each of the three federal standards each of which are slightly different from each other.

As Respondent argued to the Ninth Circuit, the decision of the Ninth Circuit is also consistent with the unanimous decisions of all Courts regarding taxes incurred

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[4] **346. Special tax provisions**

(a) Except to the extent otherwise provided in this section, subsections (b), (c), (d), (e), (g), (h), (i), and (j) of this section apply notwithstanding any State or local law imposing a tax. . . .

[5] Petitioner's Appendix 44-45.

[6] **728. Special tax provisions**

(a) For the purposes of any State or local. . . .

(b) Notwithstanding any State or local law imposing a tax on or measured by income. . . .

[7] **1146. Special tax provisions**

(a) For the purposes of any State or local law imposing a tax on or measured by income. . . .

after the commencement of the bankruptcy case which are clearly governed solely by a federal standard. Respondent's Appendix 26-27.

CONCLUSION

The Petition for Writ of Certiorari should be denied because the conflict claimed does not exist, the question contended is not raised by the facts, there is no showing that there is any state standard of proof rule applicable to these facts, the decision sought to be reviewed is correct and fair and a contrary decision would be contrary to orderly national administration of bankruptcy law.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re STEPHEN B. MACFARLANE Debtor.	CASE NOS. 94-56064 94-56065
FRANCHISE TAX BOARD OF THE STATE OF CALIFORNIA, Appellant/Cross Appellee/Creditor, -vs- STEPHEN B. MACFARLANE, Appellee/Cross Appellant/Debtor	[DC # CV-93 01435-JSR So. Dist. San Diego]

COMBINED CROSS APPEAL OPENING AND APPEAL REPLY BRIEFS OF STEPHEN B. MACFARLANE

APPEAL FROM A JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF CALIFORNIA

Honorable John S. Rhoades
United States District Judge

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STATEMENT OF ISSUES

Cross Appeal

1. Did the district court erroneously characterize the judgment of the bankruptcy court as a summary judgment? This is reviewed *de novo*.

2. If the district court correctly characterized the judgment of the bankruptcy court as a summary judgment, was there any controverted material issue of fact which prevented a valid summary judgment? This is reviewed *de novo*.

Reply to FTB Appeal

3. Was William Cheng ("Cheng") obligated to repay to Debtor the amounts of $1,400,000 and $2,028,141 advanced by Debtor to Cheng during 1988 and 1989 respectively? This is reviewed under the clearly erroneous standard.

4. Did Cheng's obligations to repay the 1988 and 1989 advances become worthless in 1988 and 1989 respectively? This is reviewed under the clearly erroneous standard.

5. Since FTB never made an assessment of the tax in question, is there any presumption of validity under state law? This is reviewed *de novo*.

6. Is a FTB proposed assessment based on an IRS' audit report which was abandoned by the U.S. Department of Justice entitled to presumptive validity? This is reviewed *de novo*.

7. Should a tax claimant be treated differently from any other claimant in the absence of any bankruptcy law or rule giving it special treatment? This is reviewed *de novo*.

STANDARD OF REVIEW

Normally review of disposition of summary judgment motions is *de novo*. The issue of whether a judgment is a summary judgment is reviewed *de novo*. This Court reviews such matters *de novo* because it is in as good a position to do so as was the district court. *In re Marquam Inv. Corp.*, 942 F.2d 1462, 1465 (9th Cir. 1991) (function of this court in reviewing district court reversal of bankruptcy court); *In re Dominguez*, 51 F.3d 1502, 1506 (9th Cir. 1995).

The district court noted that on July 12, 1993 the bankruptcy court had before it both an objection and a motion for summary judgment. Supp. ER9 and DCR11 at 6. At the hearing on the FTB's claim on March 15, 1993, the bankruptcy court continued the hearing to July 12, 1993 in order to allow the FTB an opportunity to conduct discovery and offer evidence and stated that an evidentiary hearing would be held. Supp. ER4 and DCR4 at 170.

On June 11, 1993 the Debtor filed a motion for summary determination of the claim by either evidentiary hearing or by summary judgment as the court considered appropriate. ER5 and DCR4 at 121-122. At the hearing on July 12, 1993 the court comprehensively addressed the merits of the evidence without addressing the motion for summary judgment. ER7; DCR4 at 71-81. The Debtor also noted in brief that the *de novo* standard of review should not be applied in reviewing the judgment of the bankruptcy court based on an uncontested evidentiary hearing to which no objection was made after an opportunity for discovery had been afforded. Supp. ER8 and DCR7 at 3. Finally the Debtor urged the bankruptcy court to hold that the Debtor had supported its objection by a preponderance of the evidence. ER5 and DCR4 at 128.

The characterization by the district court of the judgment of the bankruptcy court should be reviewed *de novo*. However, the findings of fact of the bankruptcy court should be reviewed under the clearly erroneous standard whether or not they were pursuant to the summary judgment motion. In reviewing a summary judgment, this Court in *Ojai Unified School District v. Jackson*, 4 F.3d 1467, 1472 (9th Cir. 1993) stated: "[T]he district court essentially conducted a bench trial based on a stipulated record. Accordingly, we conclude that, because the district court already has performed a *de facto* bench trial, a remand for trial would serve no useful purpose in this case. The parties concede that the district court had before it all of their evidence regarding the issues in dispute; the record before us is therefore complete."

Ojai involved a review of an agency determination and applied the standard of review appropriate for that

review rather than a *de novo* standard. On facts more similar to Debtor's case, this Court in *Kreisner v. City of San Diego*, 988 F.2d 883, 887n.3 (9th Cir. 1993) applied the clearly erroneous standard in an appeal from a summary judgment:

> The dissent states because we are reviewing the district court's grant of summary judgment we should view the evidence in the light most favorable to Kreisner, rather than adopt the findings of fact of the district court. . . . . Here, the district court made findings of fact after holding an evidentiary hearing and taking testimony in open court. . . . . Kreisner did not object to the holding of an evidentiary hearing, nor is there any indication that he did not have sufficient notice to present his case. . . . [T]here is no reason to depart from the clearly erroneous standard of review that we apply to findings of fact following an evidentiary hearing.

The rationale for such appellate review is stated in the Federal Judicial Center monograph on summary judgment which explains the procedure for summary judgment in a bench trial as follows:

> [W]hen the question for decision concerns drawing inferences from undisputed evidence, or interpreting and evaluating evidence to derive legal conclusions, a trial may not add to the judge's ability to decide. Thus, when the disputed issue is one of ultimate fact, a bench trial is often unnecessary; the considerations that militate in favor of trial if it is to a jury do not apply. . . . A court may determine that a full trial would add nothing to the paper record and, after proper notice, decide a case on that record,

> making a decision on a "trial without witnesses" rather than on summary judgment.

W. Schwarzer, et al., *The Analysis and Decision of Summary Judgment Motions* 39-40 (1991).

Debtor notes that the application of the clearly erroneous standard obviates the necessity to resolve the *Bonner* and *Vylene* finality issue noted in the statement of jurisdiction here.

The findings of fact of the bankruptcy court should be affirmed, as they were by the district court, unless this Court is left with "the definite and firm conviction that a mistake has been committed." If the bankruptcy court's "account of the evidence is plausible in light of the record viewed in its entirety, the court of appeals may not reverse it even though convinced that had it been siting as the trier of fact, it would have weighed the evidence differently." *Wolf v. C.I.R.*, 4 F.3d 709, 712-713 (9th Cir. 1993).

STATEMENT OF THE CASE

On June 25, 1991 the IRS issued an audit report which determined that deductions for uncollectible debts due from William Cheng in the amount of $1,400,000 for 1988 and $2,028,141 for 1989 should be disallowed and Debtor should pay income taxes, penalties and interest as of that date in the amount of $1,239,750 for 1988 and 1989. Supp. ER6 and DCR4 at 597-610. The court may take judicial notice that interest on this amount as of October 16, 1992 would add approximately $100,000 to the amount due to the IRS in addition to the 1991 amount. Accordingly as of

October 16, 1992 the amount due to the IRS was about $1,339,750.

The debtor contested the IRS claim in the bankruptcy court. On October 16, 1992 the U. S. Department of Justice conceded all but $250,000 of the IRS' $1,339,750 claim. Supp. ER6 and DCR4 at 612-614. In the meantime, on April 3, 1992 the FTB issued its notice that debtor owed $410,838 to the FTB for 1988 and 1989 income taxes, interest and penalties based solely on the IRS audit report. Supp. ER6 and DCR4 at 576, 595-596. This notice was expressly based solely upon the IRS audit report. *Id.* The FTB filed its claims in the bankruptcy court beginning in June 1992 based on that notice. Supp. ER6 and DCR4 at 576.

On January 6, 1993 Debtor's Chapter 11 plan was confirmed. ER15 at page 19 docket entry 180. On January 11, 1993 the debtor filed his objection to the FTB's claim. ER3(partial); DCR4 at 672-1154. On February 3, 1993 the FTB filed its response and set a hearing for March 15, 1993. ER4; DCR4 at 579-671. On March 2, 1993 the Debtor filed his response to the FTB's response for the hearing on March 15, 1993. Debtor raised a number of evidentiary issues. Supp. ER4 and DCR4 at 209-210.

On March 15, 1993 the bankruptcy court conducted a hearing on the Debtor's objection to the FTB claim. Supp. ER4 and DCR4 at 169-173. The court ruled that the FTB's claim was prima facie valid but that the Debtor had provided competent evidence that debts existed in 1988 and 1989 and that the debts were worthless in 1988 and 1989 rebutting the presumption of validity of the FTB claim. The court then adjourned the hearing to July 12,

1993 for an evidentiary hearing to allow the FTB to conduct discovery and offer evidence.

The FTB chose to forego discovery and offered no evidence. On June 11, 1993 the Debtor filed a motion for summary determination of the claim noting the lack of any activity by the FTB, ER5 and DCR4 at 122, and in the alternative requested that the objection to the claims of the FTB be determined on the merits on the evidence submitted. ER5 and DCR4 at 122 lines 1-3. The FTB did not respond with a statement of controverted facts or conclusions of law. It responded with a memorandum which dealt primarily with burden of proof issues. ER5 and DCR4 at 88. Debtor's position was that he had proved that loans were made to William Cheng, that they became worthless in the years claimed, that he did not have to prove that there was no evidence in existence which could lead to an alternative factual result which is apparently what the FTB argues, and that although he raised the burden of proof issue in his opening pleadings as the case had progressed the issue had become irrelevant because there were no reasonably controverted facts.

At the hearing on July 12, 1993 the bankruptcy court comprehensively addressed the issues on the merits of the evidence on the basis of the objection without addressing the summary judgment motion. ER7; DCR4 at 70-83. The court went on to criticize the FTB for failing to conduct any discovery to obtain evidence which controverted the evidence offered by the Debtor. *Id.* In neither the bankruptcy court, the district court nor here has the FTB contended that William Cheng did not obtain from Debtor $1,400,000 in 1988 and $2,028,141 in 1989. The FTB has contested only characterization of these amounts as

debts and the time of their worthlessness. The bankruptcy court's judgment, findings and conclusions were entered August 10, 1993.

The FTB filed its notice of appeal August 19, 1993. ER9. On June 29, 1994 the district court filed its memorandum decision and judgment reversing the judgment of the bankruptcy court which the district court characterized as a summary judgment, affirmed the bankruptcy court's findings as not clearly erroneous, and affirmed the court's conclusions of law. Supp. ER9. Both parties timely appealed. ER9 and Supp. ER3.

ARGUMENT

Summary

The proper standard of review of a judgment resulting from an evidentiary hearing in which all of the facts are developed is the clearly erroneous standard whether or not the hearing resulted from a motion for summary judgment. The district court was wrong when it applied a *de novo* standard of review. It was also wrong in characterizing the judgment as a summary judgment.

Even if the bankruptcy court's judgment was a summary judgment, the four aspects of evidence cited by the district court were taken out of context. The inferences drawn by the district court were not reasonable in light of all of the evidence before it. Accordingly even after a *de novo* review the district court should have affirmed.

It is uncontested that the amounts in issue were advanced to Cheng from Debtor in 1988 and 1989. All of the testimony of percipient witnesses corroborated by

inches of checks which bear notations that they are "loans", loan documents and agreements the composition and execution of which was supervised by Cheng's lawyer and statements under oath by Cheng admitting his obligation to debtor indicate the existence of a debt. The testimony of Cheng's personal bookkeeper and his office manager who managed both his affairs and debtor's affairs corroborated by his bankruptcy and subsequent valuation of his most significant asset at $2,500 amply demonstrate that at the end of 1988 and 1989 Cheng could not repay the loans. The evidence also indicates it would have been useless to pursue collection.

The Court need not resolve the issue raised by the FTB regarding the holding by the bankruptcy and district courts that the FTB is held to the same burden of proof in proving its claim which is applicable to all creditors in bankruptcy cases. The evidence is clear that even if the debtor had the burden of persuasion, he carried it. The FTB introduced no evidence and made no evidentiary objections. *It cites no relevant state standard of burden of proof after devoting more than half of its brief to an analysis of why the state standard is not preempted by federal law.* Furthermore, inasmuch as no state assessment was ever made, there is no presumptively valid assessment, and since the FTB claim was based only on an IRS report abandoned by the U.S. Department of Justice, the claim has no presumptive validity.

If the Court does decide the burden of persuasion issue, then it should note that the Supreme Court has held that the burden of proof imposed on anyone, including a tax claimant, to prove fraud in an objection to dischargeability proceeding, is different from, and less

than, the burden of proof imposed on a tax claimant outside of bankruptcy court in the assertion of fraud. The fulfillment of federal objectives mandates burdens of proof in bankruptcy cases different from other civil cases. In some instances, this burden on the government, as in the case of fraud, is lighter, and in others, as in the determination as to how the debtor's assets are to be divided among his creditors, it is heavier because all claimants should conduct their contest on a level playing field. No contrary rule is explicitly ordained. The Fifth Circuit has twice so held. The Fourth Circuit's decision to the contrary does not withstand close scrutiny and in any event was a dictum. This Court should also note that all courts agree that the holder of a tax claim arising during a bankruptcy case is not entitled to the benefit of the burden of proof applicable outside of bankruptcy court.

It is perfectly consistent with bankruptcy policy to require a tax claimant to prove entitlement in a bankruptcy case for a payment of tax from the estate, yet to the extent it is not collected from the estate and not discharged, it can be collected from the bankrupt debtor in a proceeding in which the bankrupt has the burden of proof.

Did the district court erroneously characterize the judgment of the bankruptcy court as a summary judgment subject to de novo review?

Debtor has briefed this issue of his cross appeal at pages 8 and 9 of this brief.

If the district court correctly characterized the judgment of the bankruptcy court as a summary judgment, was there a controverted material issue of fact which prevented a valid summary judgment?

The district court in reviewing the record concluded that four aspects of debtor's evidence indicated a genuine issue for trial. Supp. ER9 and DCR11 at 18-20. These are: debtor's statement Cheng did not have permission to use the debtor's money for the purposes for which it was used; debtor discussed tax shelters with Cheng; debtor couldn't distinguish loans from investments; some of the loan documents don't have repayment dates, don't bear interest rates and are not secured.

The inferences to be drawn from the evidence in favor of the FTB to defeat summary judgment must be reasonable. The permission and investment out of context statements were from two lines in 126 pages of testimony. Considering the deposition as a whole it was apparent that the debtor had loaned money to Cheng during 1988 and 1989 and that the debtor considered a loan an investment. Debtor testified that even if a bank loaned money to him the bank would be investing in him. ER6 at 135-136; DCR4 at 356-357. The only tax shelter discussion related to 1981 and 1983. ER6 at 35; DCR4 at 255-257. Neither the district court nor the FTB cited any evidence regarding tax shelters relating to the 1988 or 1989 loans. The bankruptcy court expressly noted that there was no connection shown between the tax shelters and the loans in question. ER7 and DCR4 at 77 lines 17-21. *The misrepresentation of the facts in this regard at pages 25-26 of the FTB's brief was recognized by the bankruptcy court.* The loan documents criticized by the district court, Supp. ER9 and

DCR11 at 20, were addendums to a letter loan agreement from Cheng's lawyer which clearly specified all indicia of a loan required by any criteria. Supp. ER5 and DCR4 at 549-550. The only effect of these addendums was to change one term in the letter agreement. They also related to an extensive loan agreement. Supp. ER7 and DCR4 at 1004-1017.

Arrayed against these four out of context references was all of the other evidence regarding existence of debt and worthlessness discussed *infra*.

Debtor suggests that construing the entirety of the record the only reasonable conclusion one can come to is that Cheng borrowed during 1988 and 1989 not only the amounts in issue, but more than that amount, and that the loans made during 1988 and 1989 were worthless at the end of each of these years. Also, as pointed out *infra*, even if these loans were investments, they clearly were made for profit and if worthless would result in a capital loss which is what debtor claimed. This issue was raised in bankruptcy court by the debtor. ER5 and DCR4 at 128. Whether the loss occurs under I.R.C. 165 or 166 is not a distinction with a difference here. Because a judgment may be affirmed on any basis which appears from the record, the district court should have affirmed the judgment of the bankruptcy court.

Was William Cheng ("Cheng") obligated to repay to Debtor the amounts of $1,400,000 and $2,028,141 advanced by Debtor to Cheng during 1988 and 1989 respectively? Did Cheng's obligations to repay the 1988 and 1989 advances become worthless in 1988 and 1989 respectively?

The evidence offered by the Debtor, to which no evidentiary objections from the FTB were made notwithstanding the FTB's complaints about hearsay in its brief, included:

1. Leslie Szutenbach worked with Debtor and Cheng in all aspects of their business affairs during 1988 and 1989 and is a percipient witness with personal knowledge of such affairs and is the custodian of the documents offered and the person in the course of whose business the documents were prepared on the dates shown on them. Supp. ER6 and DCR4 at 736-778, 837-838, 852, 854(top), 855, 857, 868(top); Supp. ER7 and DCR4 at 874, 877, 882(top), 884(top), 887(top), 888-891, 892(top), 896, 897, 907, 914-918, 1017 and 1027.

2. By December 31, 1988 Cheng had obtained at least $1,632,500 from Debtor and promised to repay this amount. Supp. ER6 and DCR4 at 701, 712, 737, 753, Supp. ER7 and DCR4 at 916-918, 1028-1030, 1033 and 1038.

3. In 1989 Cheng obtained at least $2,224,077 from Debtor and promised to repay this amount. Supp. ER6 and DCR4 at 701, 702; Supp. ER7 and DCR4 at 1028 and 1038.

4. On December 31, 1988 and December 31, 1989 Cheng's promises to pay were worthless. Supp. ER6 and DCR4 at 701 and 702.

5. Cheng knew when he prepared Debtor's 1988 and 1989 federal income tax returns that he could not repay these amounts and therefore caused Debtor's 1988 and 1989 federal income tax returns to report bad debt losses for $1,400,000 for 1988 and $2,028,141 for 1989. Supp. ER6 and DCR4 at 743-744 and 702.

6. In April 1991 Cheng commenced a bankruptcy case under Chapter 13 of Title 11 U.S.C. and his case was converted to Chapter 7 in May 1991. Supp. ER6 and DCR4 at 702 and 703.

7. Cheng's bankruptcy estate has little or no value. Supp. ER6 and DCR4 at 702, 723 and 725.

8. The primary asset of his estate was stock in Cheng Information Systems, Inc., all of the property of which was sold by CIS' bankruptcy trustee for $2,500. Supp. ER6 and DCR4 at 702 and 725.

9. As of December 31, 1988 and December 31, 1989 Macfarlane had no realistic prospect of recovery from Cheng of any of the amounts then due to Macfarlane. Supp. ER6 and DCR4 at 702.

10. John Haegen and Leslie Szutenbach assisted in the preparation of Debtor's 1988 and 1989 tax returns. Supp. ER5 and DCR4 at 316-317; Supp. ER7 and DCR4 at 1026 and 1028. John Haegen was a custodian of the records which evidence the loans and summarized them. Supp. ER7 and DCR4 at 1026-1034. Summary at Supp. ER7 and DCR4 at 1038 with detail appended. Supp. ER5 and DCR4 at 316-317, 332 line 1.

11. Debtor gave Cheng a general power of attorney in 1983, Supp. ER5 and DCR4 at 290-294, and 418 to 421,

and numerous special powers of attorney. Supp. ER5 and DCR4 at 275-289.

12. Cheng signed Debtor's 1988 and 1989 returns as their preparer. Supp. ER5 and DCR4 at 272, 312, 325, 423, and 471.

13. Debtor claimed a $1,400,000 bad debt for 1988, Supp. ER5 and DCR4 at 433, and a $2,028,141 bad debt for 1989. Supp. ER5 and DCR4 at 516.

14. Leslie Szutenbach was a percipient witness for all of the circumstances surrounding the loans from Debtor to Cheng. Supp. ER5 and DCR4 at 262-264, 266, 267, 274.

15. Debtor and Cheng signed documents evidencing an intent to enter into a debtor and creditor relationship. Supp. ER5 and DCR4 at 350, 351, 358 through 364, and 547 through 559. See also Supp. ER6 and DCR4 at 772, 775 and Supp. ER7 and DCR4 at 1000-1018.

16. Cheng was in dire financial straits in 1988 and by the end of 1989 was living off loans. Supp. ER5 and DCR4 at 560-564.

17. Cheng managed all of Debtor's property and affairs and Debtor trusted Cheng for all financial advice. Supp. ER5 and DCR4 at 252-254, 275, and in particular, 298 through 311. Debtor had a mental breakdown in 1980 or 1981, and after that Debtor relied on Cheng to conduct his affairs. Supp. ER5 and DCR4 at 245-248.

18. Debtor loaned $2,047,232 to Cheng in 1989. Supp. ER5 and DCR4 at 337-338.

19. Debtor loaned a total of $4,529,349 to Cheng. Supp. ER5 and DCR4 at 412.

The substantive tax law issues have been decided based on federal law because of California's conformity to federal law on this subject. In this regard it is important to note the Debtor has noted that the loss claimed by Debtor was a nonbusiness bad debt, or capital, loss. Consequently the FTB's emphasis on characterizing the loan in question as an "investment" does not change the income tax result if worthlessness nevertheless occurred in 1988 and 1989 as contended by Debtor. The tax in question arose from capital gains which were offset by the capital loss at issue. Supp. ER6 and DCR4 at 598-610; ER5 and DCR4 at 128. The bankruptcy court at the July 15, 1993 hearing systematically addressed the criteria for deductibility of bad debt losses listed by the FTB in the context of the evidence offered by the Debtor. As the court noted, the amounts involved were not in issue. The bankruptcy court started its analysis with the letter of January 12, 1987, Supp. ER5 and DCR4 at 547-548, which clearly reflected a secured loan transaction in the amount of $250,000. On February 26, 1987 there is memorialization of an offer by Debtor to lend to Cheng an amount of $500,000 witnessed by Leslie Szutenbach. Supp. ER5 and DCR4 at 549. This was increased to $750,000 on May 6, 1987. Supp. ER5 and DCR4 at 550. Debtor wrote checks to Cheng for the loans. Supp. ER5 and DCR4 at 551-556. Cheng signed promissory notes. Supp. ER5 and DCR4 at 557-559. Some of these same documents, and additional documents, are at Supp. ER7 and DCR4 at 1004-1018. On July 31, 1988 Debtor and Macfarlane entered into a loan agreement which acknowledged loans of up to $1,250,000

and granted Debtor the right to exchange his right to repayment from Cheng to a right of repayment from a corporation upon the occurrence of events which never transpired and expressly acknowledged that the agreement did not require the Debtor to enter into such an exchange or to limit Cheng's obligation to repay the debt to Debtor. Supp. ER7 and DCR4 at 1004-1017. At Supp. ER7 and DCR4 at 1009 is a letter from Cheng's lawyer who characterized the transactions involved as loans by Debtor to Cheng. In addition to these documents are the checks all of which were designated as loans to Cheng by Debtor and Cheng and summarized by Szutenbach in her declaration and deposition and by John Haegen in his summary of the net checks written to Cheng as loans from Debtor. As to Haegen, see Supp. ER7 and DCR4 at 1038. As noted, the amounts are not in issue and the intent to create a debtor-creditor relationship is well established by Cheng's bankruptcy schedules which show him indebted to Debtor in the amount of $2,939,722 and as owning all of the stock of Cheng Information Systems, by the declaration of Szutenbach and by her deposition and by the Debtor's deposition which include as exhibits the many documents which evidence a debtor-creditor relationship and by the Debtor's tax returns prepared by Cheng and by Cheng's own statements reflected in the depositions and declarations in the record. Cheng's bankruptcy schedules also indicate that there were other lenders loaning money to him during the periods in issue contrary to the FTB's argument that Macfarlane was the only lender. Supp. ER6 and DCR4 at 708-714.

The evidence regarding Cheng's inability to repay these loans as of the end of 1988 and 1989 is uncontradicted. His personal bookkeeper's declaration substantiates his inability to repay. Supp. ER6 and DCR4 at 560-564. He repeatedly stated to Szutenbach than [sic] he could not repay. Supp. ER6 and DCR4 at 743 lines 19-20 and 744 lines 2 and 13. The assets of his only significant asset, Cheng Information Systems, sold for $2,500. Supp. ER6 and DCR4 at 702 and 725. He prepared and signed as preparer the Debtor's tax returns in which he admitted the existence of the debts at issue here and their worthlessness. Supp. ER5 and DCR4 at 423 and 471. Cheng's admissions in this record are uncontradicted. The FTB's inordinate reliance on the circumstance that Cheng had Debtor's power of attorney doesn't contradict any evidence offered by Debtor; it simply confirms, as the bankruptcy court indicated, that Cheng had the authority to carry out the agreements or otherwise to loan the Debtor's funds. As to the FTB's argument that the loans had to have value when made, the Debtor argued that loans can become worthless when made as indicated by the IRS' policy because debts are created both by law and by contract. Supp. ER4 and DCR4 at 214-216. The bankruptcy court stated that was not a problem because at least at the time the loan was made it could have been repaid with the loan proceeds.

As to the FTB's statement on page 28 (bottom) of its brief, that there is "absolutely no evidence . . . that Cheng ever attempted to repay Macfarlane," this is not absolutely true. John Haegen's summary of loans to Cheng was a summary of "net" loans because Cheng did make payments to Macfarlane in 1988. Supp. ER6 and DCR4 at

788; Supp. ER7 and DCR4 at 1038, 1041. This misrepresentation is similar to statements such as the one on page 29 (bottom) of the FTB brief that "the only evidence to support Cheng's inability to repay Macfarlane's cash advances was a hearsay statement from Szutenbach, a former Cheng employee. . . . " As the record amply shows, Szutenbach was Cheng's office manager and her initials are on many of the significant documents in evidence. She also was in charge of Macfarlane's affairs. The FTB made no hearsay objection. But her statement is not the only evidence. The FTB overlooks the declaration of Cheng's personal bookkeeper who had percipient personal knowledge of his financial affairs, the inferences one can gather from Cheng's bankruptcy schedules, and his admissions. See discussion in the preceding paragraph.

The FTB's reliance on a requirement of an "identifiable event" rendering the loan worthless in making the claim, Supp. ER6 and DCR4 at 576 lines 27-28, and in its brief, is simply not the law. There does not have to be an identifiable event; the taxpayer must simply persuade the court that the debt became worthless at the necessary time.

Debts are wholly worthless when there are reasonable grounds for abandoning any hope of repayment in the future, *Dallmeyer v. Commissioner*, 14 T.C. 1282, 1292 (1950), and it could thus be concluded that they have lost their "last vestige of value." *Bodzy v. Commissioner*, 321 F.2d 331, 335 (5th Cir. 1963). But a taxpayer need not be "an incorrigible optimist." *United States v. S.S. White Dental Manufacturing Co.*, 274 U.S. 398, 403, 47 S. Ct. 598, 600 (1927). This will usually entail proof of the existence of

identifiable events which demonstrate the valuelessness of the debts. *Riss v. Commissioner*, 478 F.2d 1160 (8th Cir. 1973); *Crown v. Commissioner*, 77 T.C. 582, 598 (1981); *Hubble v. Commissioner*, 42 T.C.M. 1537, 1544 (1981). *Estate of Mann*, 731 F.2d 267, 276 (5th Cir. 1984). However, when or whether a debt becomes worthless is a question of fact, the answer to which lies in an examination of all the circumstances. *Boehm v. Commissioner*, 326 U.S. 287, 293 (1945); *Estate of Mann*, 731 F.2d 267, 275 (5th Cir. 1984); *Dallmeyer v. Commissioner, supra* at 1291. When a debt becomes worthless is to be decided by the trier of fact. *Cole v. Commissioner*, 871 F.2d 64, 66 (7th Cir. 1989), *aff'g.* T.C. Memo. 1987-228. A bad debt is deductible only in the year it becomes worthless. *Denver & Rio Grande Western Railroad Co. v. Commissioner*, 32 T.C. 43, 56 (1959), *aff'd.* 279 F.2d 368 (10th Cir. 1960); *Feinstein v. Commissioner*, 24 T.C. 656, 658 (1955). Worthlessness is determined by objective standards. *Perry v. Commissioner*, 22 T.C. 968, 973 (1954). Some factors that have been considered by courts in determining worthlessness include the subordinated status of the debt (*Cole v. Commissioner, supra* at 67); a decline in the debtor's business (*Continental Illinois National Bank & Trust Co. of Chicago v. United States*, 81-1 USTC par. 9185 (N.D. Ill. 1981)); the decline in value of the property secured by the debt (*Meurer Steel Barrel Co., Inc. v. Commissioner*, 7 B.T.A. 64, 66 (1927)); claims of prior creditors far in excess of the fair market value of all assets available for payment (*Hadley Falls Trust Co. v. United States*, 110 F.2d 887, 890-891 (1st Cir. 1940)); the overall business climate, the debtor's earning capacity, the debtor's serious financial reverses, guarantees on the

debt, events of default, whether major or minor, insolvency of the debtor, the obligor's refusal to pay, abandonment of assets or business, ill health, death, or disappearance of the principals, bankruptcy or receivership, actions of the obligee in pursuing collection, i.e., whether the obligee unreasonably failed to take collection action and then claimed the deduction, subsequent dealings between the obligee and obligor, and lack of assets (*Cole v. Commissioner, supra*).

No single factor is conclusive as there are no absolutes in this area. *See* 2 B. Bittker & L. Lokken, *Federal Taxation of Income, Estates and Gifts*, sec. 33.3.1, pp. 33-10 to 33-11 (2d ed. 1990). Default is a factor considered in deciding whether an obligation is worthless. *Cole v. Commissioner, supra*. However, the fact that a debt had not matured does not prevent a finding of worthlessness. *Bonynge v. Helvering*, 117 F.2d 157, 158 (2d Cir. 1941), *aff'g.* 41 B.T.A. 84 (1940); *Robert Smith Corp. v. Commissioner*, 21 B.T.A. 1400, 1405 (1931). Similarly, the fact that a bad debt is not due at the time of deduction does not of itself prevent its allowance under section 166. Sec. 1.166-1(c)(7), Income Tax Regs. A taxpayer need not wait for a default before taking a bad debt deduction if the debt is clearly worthless before any payments are due. *Bonynge v. Helvering, supra* at 158.

Legal action is not required before a bad debt deduction is allowable where the surrounding circumstances indicate that a debt is worthless and uncollectible and that legal action to enforce payment would in all probability not result in the satisfaction of execution on a judgment. However, a showing of these facts will be sufficient evidence of the worthlessness of the debt for

purposes of the deduction under section 166. Sec. 1.166-2(a) and (b), Income Tax Regs.; *Exxon Corp. v. United States*, 785 F.2d 277, 279 (Fed. Cir. 1986). In determining worthlessness, no one factor is controlling.

It is obvious that there is no precise test for determining worthlessness within the taxable year and neither the statutory enactment, its regulations, nor the decisions attempt such an all-inclusive definition. Furthermore, it is often impossible to select a single factor or "identifiable event" which clearly establishes the time at which a debt becomes worthless and thus deductible. *Minneapolis, St. Paul Railroad Co. v. United States*, 164 Ct. Cl. 226, 240 (1964). All pertinent evidence should be considered. Sec. 1.166-2(a), Income Tax Regs. See also *Estate of Mann*, 731 F.2d 267, 276-277 (5th Cir. 1984):

> Subsequent events may only be used to evaluate the soundness of the belief that a debt became worthless in a certain year, and not as evidence of the fact of worthlessness. . . . The fact that a debt reasonably determined to be worthless in a given taxable year, is subsequently recovered in part or in full, is not in itself sufficient to prevent the deduction. . . .
>
> If and when such a debt becomes wholly worthless must be determined from the facts and circumstances known or which *reasonably could have been known at the end of the year of asserted worthlessness*. . . . Of course, proof of subsequent events may be allowed, as they were here, insofar as they may be relevant to the reasonableness of a conclusion that a debt became worthless in the particular year. . . .

Id. at 278 and n. 19. (Emphasis added)

In this case we have percipient witnesses' testimony. Also subsequent events, such as the demonstrable worthlessness of Cheng's bankruptcy estate, can be taken into account under *Mann* to assess the reasonableness of a determination of worthlessness in 1988 and 1989.

The findings of the bankruptcy court are not only not clearly erroneous, but are clearly supported by uncontroverted evidence. The conclusions are appropriate under the law.

Since the FTB never made an assessment of the tax in question, is there any presumption of validity under state law?

The FTB notice of proposed assessments were issued on April 3, 1992, almost two years after the Debtor commenced his bankruptcy case in 1990, at a time when the FTB knew that the IRS audit report was being contested in the bankruptcy court. Supp. ER6 and DCR4 at 576-577, 595-596, 612-613 (attachment to FTB pleading). The FTB did not, and because of the automatic stay under 11 U.S.C. § 362, could not, assess the tax in question. Accordingly there is no assessment by the FTB to which presumptive validity can attach. Although most of the FTB's brief is dedicated to arguments why state law relating to burden of proof should govern in this case, the FTB's brief never tells this Court what state law governs. At page 12 of its brief the FTB cites two decisions holding that in refund claim litigation in state court the taxpayer has the burden of proving the right to repayment of a tax the taxpayer has paid. *Nowhere does the FTB tell this Court what state law imposes upon the taxpayer the burden of proving the lack of validity of an unassessed state tax based on an*

abandoned IRS report. This Court may hold that the FTB has waived its argument on this issue.

Is a FTB proposed assessment based on an IRS audit report which was abandoned by the U.S. Department of Justice entitled to presumptive validity?

The FTB's attempt to make this a test case to establish in this circuit whether or not the procedural bankruptcy claims allowance rules applicable by their terms to everyone apply to tax collectors fails if the claim of the FTB is not entitled to presumptive validity. As noted above all that the FTB did was adopt an IRS audit report which was being contested in bankruptcy court and which was later replaced by a stipulation in bankruptcy court settling the IRS claim essentially for the costs of litigation. Even after the audit report had been abandoned by the U.S. Department of Justice the FTB continued to rely on it for its proof of claim. The FTB admitted that it conducted no audit or investigation or made any inquiry beyond the IRS audit report. Supp. ER6 and DCR4 at 576-577. On these facts the presumptive validity of the FTB's claim would be subject to doubt in any court. In *Portillo v. C.I.R.*, 932 F.2d 1128 (5th Cir. 1991) the court held that the IRS' assessment based on an information return filed by a person who paid the taxpayer money was not a "determination" and the assessment was not entitled to presumptive validity. The FTB relied on information received from another person without making any independent determination as did the IRS in *Portillo* and the result should be the same; the FTB claim should have no presumptive validity. This is particularly true on the facts of this case which include the repudiation of the information upon which the FTB relied.

Should the determination of the validity of the claim of a tax claimant be conducted differently from the determination of the validity of the claim of any other claimant in the absence of any bankruptcy law or rule giving it special treatment?

If this Court concludes, as Debtor contends, that even if he had the burden of proving his entitlement to the deductions, he has carried it, then most of the FTB's brief is not material to the issues which have to be resolved in this appeal.

It is apparent that the FTB, and other commentators, have not analyzed all of the possible consequences of the contention that the allocation of burden of proof outside of bankruptcy court should govern allocation of burden of proof in bankruptcy court. For example, outside of bankruptcy court the government must prove civil fraud by clear and convincing evidence. *Ackland v. C.I.R.*, 767 F.2d 618 (9th Cir. 1985). But in bankruptcy court the government must prove civil fraud only by a preponderance of evidence. *Grogan v. Garner,* 111 S.Ct. 654 (1991). It is clear that federal objectives modify for bankruptcy purposes burden of proof rules otherwise applicable. Regarding fraud, the modification is to the government's benefit; regarding competing with other creditors for a debtor's assets in the claims allowance process, the modification creates a level playing field. The tax claimant, as well as all other claimants, should have to prove entitlement to priority and amount by a preponderance of the evidence.

The Court should be aware that all courts who have addressed the issue agree that a tax claim arising during a bankruptcy case is not entitled to any presumptive

validity. *In re Fullmer*, 962 F.2d 1463, 1467 (10th Cir. 1992); *In re Glen Eden Hosp., Inc.*, 172 B.R. 538 (Bk. E.D. Mich. 1994); *In re Allen Care Centers, Inc.*, 163 B.R. 180 (Bk. D. Or. 1994). In these cases the courts held that absent the application of F.R.B.P. 3001(f), tax claimants are not entitled to the burden of proof allocation applicable outside of bankruptcy court. If the FTB's argument is correct, then these decisions are wrong.

The Fifth Circuit in *In re Placid Oil Co.*, 988 F.2d 554 (5th Cir. 1993) held that tax claims were to be determined just like any other claim insofar as burden of proof was concerned. While tax claims are granted priority when allowed, the bankruptcy code does not specify any special advantage which tax authorities have in the claims allowance process. *Accord, California State Board of Equalization v. Official Unsecured Creditors Comm. (In re Fidelity Holding Co., Ltd.)*, 837 F.2d 696 (5th Cir. 1988).

In addition to the absence of any express statutory advantage, it has been argued, and it is true, that it is not the taxpayer and the tax collector who are at issue in a tax claim contest in bankruptcy court, but rather the estate and the tax collector. It happens that in this case the Debtor is the representative of the estate. As provided by 11 U.S.C. § 1107(a) he acts as trustee for the estate. If the estate were represented by a trustee, as happens in every Chapter 7 case and many Chapter 11 cases, who was not the Debtor most of the arguments made by the FTB relating to access to information here would be groundless. *The bankruptcy code does not allocate burdens of proof dependent on whether one person or the other is trustee of an estate.* The primary authority relied on by the FTB indeed did involve a trustee who was not the debtor. *Internal*

Revenue Service v. Levy (In re Landbank Equity Corporation), 973 F.2d 265 (4th Cir. 1992). In that case neither the tax collector nor the trustee had access to the relevant factual evidence. This distinction with a difference exists even in refund claim litigation in federal district courts in which substantive law is disregarded in some contexts because the parties before the court are different from the parties between whom the law regulates substantive relations.

It is apparent that *Levy* overstated the authorities upon which it relied and that its holding regarding burden of proof is a dictum. In that case the claim was prima facie valid, as it is here, and the trustee offered no evidence in opposition. No new law needed to be pronounced by the Fourth Circuit to hold for the tax collector. Furthermore, the references to legislative history and interpretations of the court in *Levy* were simply wrong. The erroneous statements of the court in *Levy* simply do not detract from the result required by the difference in parties before the court and outside the court, the language of the bankruptcy code which states that there shall be a priority for certain claims when they are allowed but specifies no advantage for the tax collector in the allowance process, the interpretation of United States Supreme Court decisions relating to claims allowance and determinations in the bankruptcy court summarized and analyzed hereafter, and two decisions of the Fifth Circuit which do expressly address this issue one of which involves a California state tax collector. It is well established that although state law determines property rights, federal bankruptcy law determines both the manner and the time in which such rights are to be determined and the federal consequences to be attached

to such property rights. The FTB's argument first that the burden of proof under state law in state courts is akin to a property right and second that it is governing in determining whether another creditor of a bankruptcy estate gets less simply because a tax claim rather than a nontax claim of the same amount is asserted doesn't seem to be consistent with the federal bankruptcy policy reflected in the statutes and Supreme Court decisions which bear on this subject. The FTB's ubiquitous citations to *Vanston Bondholders Protective Comm. v. Green,* 329 U.S. 156, 67 S. Ct. 237 (1946) in support of its position fail to quote the most relevant passage from the opinion: "In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state where it sits." *Id.* at 329 U.S. 162. It should also be noted that in addition to the substantive decisions regarding the paramount nature of federal law in bankruptcy cases, a strong argument can be made that the FTB in filing its claim consented to a federal burden of proof rule. *See also,* E. Martin, *Consent: The Constitutional Basis for Bankruptcy Judge Authority,* 19 Cal. Bankr. J. 1 (1991).

Debtor contends that the FTB must bear the ultimate burden. *In re Federated Department Stores, Inc.,* 135 B.R. 950, 957-58 (Bk. S.D. Ohio 1992): "This Court finds that the better reasoned cases are those that treat the government as any other creditor in bankruptcy, and accordingly, place the burden on the IRS to establish its claim. . . . These decisions hold that the government must be treated like any other claimant in bankruptcy court and is not entitled to any special exception." *See also In re Premo,* 116 B.R. 515 (Bk. E.D. Mich. 1990); *In re Compass*

Marine Corp., 146 B.R. 138 (Bk. E.D. Pa. 1992); *In re Rasbury*, 130 B.R. 990 (Bk. N.D. Ala. 1991), *aff'd* 141 B.R. 752 (N.D. Ala. 1992); *In re Dakota Industries*, 131 B.R. 437 (Bk. S.D. 1991) ("The Court concludes that 11 U.S.C. § 502(a)'s allocation of the burden of proof applies in tax assessments."); *In re Imperial Corporation of America*, 91-2 USTC ¶ 50,342, [1990-1991 Transfer Binder] Bankr. L. Rep. (CCH) ¶ 74,096 at 99,759 (Bk. S.D. Cal.).

In a claims contest it is the objection which is heard, not the claim, *Controller of California v. Lockwood*, 193 F.2d 169, 171 (9th Cir. 1952) citing *Whitney v. Dresser*, 26 S. Ct. 316, 317 (1905), yet the burden of persuasion is on the claimant. Furthermore, the Debtor may file a claim and object to it. *Kilen v. United States (In re Kilen)*, 129 B.R. 538 (Bk. N.D. Ill. 1991).

In *Internal Revenue Service v. Levy (In re Landbank Equity Corporation)*, 973 F.2d 265 (4th Cir. 1992), the issue was whether the trustee of a Chapter 7 estate had the burden of proving that the estate was entitled to a bad debt deduction from income of the estate. The issue arose in the context of a claim by the IRS for prepetition taxes which was first agreed to by the trustee but which he later sought to have disallowed. The factual issue involved was the year in which debts became worthless. It was impossible for either the trustee or the IRS to show in which years the debts became worthless; accordingly the issue of who had the burden of proving the timing of the worthlessness was determinative of the controversy.

The court in *Levy* in very broad terms held that the burden of proof rules which would have applied in a

nonbankruptcy forum, should also apply in the bankruptcy forum and there existed no equitable reason why the nonbankruptcy forum rule should not be applied.

The Debtor here argues that the result in *Levy* was arguably correct because the IRS' claim was entitled to prima facie validity under F.R.B.P. Rule 3001(f) and there was no evidence to rebut the prima facie validity of the claim. However, the additional reasons for its decision stated by the court were dicta, and the court clearly failed to accurately apply governing precedents and erroneously characterized the historical treatment of tax claims in bankruptcy, since the 1938 Chandler Act first obligated tax authorities to file claims in bankruptcy cases. The burden of proof rule is in any event a rule which by its terms applies only in a controversy between a taxpayer and a taxing agency and in this case and in every bankruptcy case the controversy is between the taxing agency and other creditors of the Debtor. The equitable objective of equality in treatment in bankruptcy distributions requires that the taxing agencies and other creditors compete on an equal footing governed by only the rules in bankruptcy cases and not by presumptions and burdens of proof which apply in controversies which are not in a bankruptcy context.

The customary IRS burden of proof argument outside of a bankruptcy case is set forth in *United States v. Molitor*, 337 F.2d 917, 922-923 (9th Cir. 1964):

> When, therefore, an assessment has been made by this officer it is to be presumed until such presumption is overcome by proof to the contrary that it was made upon sufficient evidence. . . . Such an assessment is not, however,

> conclusive evidence of the liability of the distiller; it is open to attack; it is prima facie proof only of such liability, and prima facie evidence is such evidence as is sufficient, when unassailed, to establish a given fact, and it remains sufficient for that purpose until it is rebutted and overcome.
>
> And upon it being so made to appear, the burden of proof then shifts to the plaintiffs [the IRS], and it then becomes incumbent on the plaintiffs to maintain and establish the correctness of the assessment. . . .

This prima facie validity standard is not different from the bankruptcy standard under F.R.B.P. Rule 3001(f) which the court could have chosen to apply in *Levy* rather than expound as it did on issues which were not germane to the decision. In *United States v. Sampsell*, 224 F.2d 721, 722-23 (9th Cir. 1955), the Ninth Circuit disposed of a controversy similar to that in *Levy* by simply saying: "[A] sworn proof of a tax claim in proper form establishes a prima facie case for the allowance of the claim. The burden of proof is on the claimant, but the burden of going forward and introducing evidence to rebut the prima facie case is on the objecting party. The trustee has not met this burden."

It should also be noted that procedural burden of persuasion differs somewhat in each of the three federal courts with jurisdiction in tax matters. If a uniform burden of persuasion standard is to be adopted, which is more appropriate than another? To paraphrase *Cheng v. Gill (In re Cheng)*, 943 F.2d 1114, 1117 (9th Cir. 1991), the rule applied should be one which is most apparent and in this case it is the standard simply of F.R.B.P. 3001(f).

Accordingly, it appears that if the *Levy* court had limited its holding to the holding dispositive of the case, the same result would have obtained from merely the application of F.R.B.P. 3001(f) without the verbal embroidery to which most of the opinion is devoted and since F.R.B.P. 3001(f) most specifically applies to this issue, it should govern.

The opinion in *Levy* states that substantive law applies in determining the validity of claims against a bankruptcy estate. Again, the Debtor in the case at bar agrees with the rule but not how it has been applied. *Levy* cites *Dick v. New York Life Ins. Co.*, 359 U.S. 437, 446 (1959) as holding that burden of proof rules are "substantive" and that therefore they are applicable in tax determinations in bankruptcy court. *Dick* was an accidental death diversity jurisdiction case, not a federal jurisdiction case in which substantive law, state or federal, was sought to be applied. *Dick* merely held at the cited page that "[u]nder the *Erie* rule, presumptions (and their effects) and burden of proof are 'substantive' and hence respondent was required to shoulder the burden during the instant trial."

Perhaps a more appropriate starting point for the analysis of the applicability of the "outside of bankruptcy court" burden of proof rule in bankruptcy court would have been *Grogan v. Garner*, 111 S.Ct. 654, 657-658&n.9 (1991) in which the court said:

> At the outset, we distinguish between the standard of proof that a creditor must satisfy in order to establish a valid claim against a bankruptcy estate and the standard that a creditor who has established a valid claim must still

> satisfy in order to avoid dischargeability. The validity of a creditor's claim is determined by rules of state law. See *Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 161, 67 S.Ct. 237, 239, 91 L.Ed. 162 (1946). Since 1970, however, the issue of nondischargeability has been a matter of federal law governed by the terms of the Bankruptcy Code. . . .

In *Vanston*, cited in *Grogan* as announcing the ultimate rule governing the issue in the case at bar, the Court did what the *Levy* court said it was not empowered to do: it denied the allowance of a claim without regard to state law because state law could not contravene the overriding bankruptcy objective of equality and equity in distribution.

> A purpose of bankruptcy is so to administer an estate as to bring about a ratable distribution of assets among the bankrupt's creditors. What claims of creditors are valid and subsisting obligations against the bankruptcy at the time a petition in bankruptcy is filed, is a question which, in the absence of overruling federal law, is to be determined by reference to state law. . . . [A]ssuming, arguendo, that the obligation for interest on interest is valid under the law of New York, Kentucky, and the other states having some interest in the indenture transaction, we would still have to decide whether allowance of the claim would be compatible with the policy of the Bankruptcy Act. . . . *In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state where it sits.* . . . Bankruptcy courts must administer and enforce the Bankruptcy Act as interpreted by

> this Court in accordance with authority granted by Congress to determine who and what claims shall be allowed under equitable principles. . . . It is manifest that the touchstone of each decision on allowance of interest in bankruptcy, receivership and reorganization has been a *balance of equities between creditor and creditor* or between creditors and the debtor. . . . (emphasis added)

Id. at 67 S. Ct. 239-241 and note 5. Ironically, the Fourth Circuit held that "*Vanston's* vitality has not diminished," *In re Twin Parks Ltd. Partnership*, 720 F.2d 1374, 1377 (4th Cir. 1983), and it applied the preemption standard of *Vanston* to define a "claim" in *Grady v. A.H. Robins Co., Inc.*, 839 F.2d 198, 201-202 (4th Cir. 1988), again to do what it said in *Levy* it could not do. And an examination of the decisions relied on in *Vanston* indicates that *Vanston* was not the first decision to determine the allowability of a claim by reference to the equitable objectives of the bankruptcy laws. Judge Ryan in *In re DWS Investments, Inc.*, 121 B.R. 845 (Bk. C.D. Cal. 1990) likewise applied *Vanston* to achieve a equitable distribution and in *Southwest Bank v. Parsons (In re Parsons)*, 124 B.R. 818 (Bk. S.D. Cal. 1991) the court cited both *Grogan* and *Vanston* in deciding the issue before the court. The Ninth Circuit in *Official Cattle Contract Holders Committee v. Commons (In re Tedlock Cattle Company, Inc.)*, 552 F.2d 1351, 1352-1353 (9th Cir. 1977) did likewise in declining to follow California law in allowing a claim applying instead equitable bankruptcy principles and in *United States v. Robinson (In re D.C. Sullivan & Co., Inc.)*, 929 F.2d 1, 6 (1st Cir. 1991) the court noted that the *Ron Pair* decision adopted the *Vanston* approach.

Accordingly it is apparent that although state substantive law must be applied to determine the "substantive rights" of the claimant, it is not so apparent whether the burden of persuasion rule should be applied if it causes a deviation from the objective that all claimants should be treated alike. *Levy* asserts that because government claimants have always been given the burden of proof in bankruptcy cases which they would have had outside of the bankruptcy case, Congress did not intend to change such application. However, the authority cited by *Levy* for the proposition that governments have been given the benefit of more than a prima facie validity of their claims consists of decisions in which the issue wasn't raised, *Resyn Corp. v. United States*, 851 F.2d, 660, 662-63 (3rd Cir. 1988); *United States v. Uneco, Inc. (In re Uneco, Inc.)*, 532 F.2d 1204, 1207 (8th Cir. 1976), followed by a "but see" signal to *California State Bd. of Equalization v. Official Unsecured Creditors Comm. (In re Fidelity Holding Co., Ltd.)*, 837 F.2d 696, 698 (5th Cir. 1988) in which the issue was raised and in which it was held that a California taxing agency should be treated just like any other claimant without the benefit of any special advantage available to it under state law. Consequently one must look elsewhere to ascertain what the historical treatment of tax claims has been in bankruptcy cases to ascertain what it was that Congress did or did not intend to change.

The standard treatise on the Bankruptcy Act, 3A J. Moore, *Collier on Bankruptcy* ¶ 64,409 at 2244 (14th ed. 1988) states: "As in the case of other types of claims, a filed proof of a tax claim in proper form establishes a prima facie case for the allowance of the claim. The

burden of proof is on the claimant, but the burden of going forward and introducing evidence to rebut the prima facie case is on the objecting party. In *Nicholas v. United States*, 86 S. Ct. 1674, 1679 n.4 (1966) the Court notes that "in 1938, however, Congress amended the Bankruptcy Act by reducing tax debts to the status of a fourth priority . . . and by requiring tax claims to be proved in the bankruptcy proceeding like ordinary debts . . . In *Saper*, the Court held that, in light of these amendments, tax debts had become sufficiently clothed with the characteristics of other bankruptcy debts to justify the application of the general rule. . . . "

Similarly see *Heiser v. Woodruff*, supra, 66 S. Ct. at 860 n.1 (1946) which was relied on by *Vanston* and *Note, Taxation During Bankruptcy Liquidation*, 55 Harv. L. Rev. 1141, 1146 (1942).

There is very little to indicate that tax claims were given the benefit historically of more than the prima facie validity accorded to all claims when the issue was relevant. As noted in *United States v. Sampsell*, 224 F.2d 721 (9th Cir. 1955), it appeared that the court assumed the customary bankruptcy standard applied. In *Dickinson v. Riley*, 86 F.2d 385 (8th Cir. 1936) the court expressly held that presumptive validity under state law would not govern the allowability of a tax claim in a bankruptcy case. *New Jersey v. Anderson*, 27 S. Ct. 137, 140 (1906) held that state law characterization of a state exaction as a tax was not governing for purposes of classifying the exaction as a tax entitled to priority. In *Industrial Commission of Ohio v. Highway Const. Co. of Ohio*, 105 F.2d 863, 866 (6th Cir. 1939), the state argued that its state statute should govern the prima facie validity of its claim. The court rejected

that position and stated that the customary bankruptcy standard applied to determine the validity of the claim. Likewise in *In re Hotel Martin Co. of Utica*, 41 F. Supp. 392 (N.D.N.Y. 1941) the court dealt with a claim for taxes as if only the bankruptcy procedures for claim allowance governed and restrained recourse to any state procedures for determination of the claim. These authorities are considerably more persuasive than the authorities cited by *Levy* except for the "but see" reference in *Levy* to the Fifth Circuit decision which holds against *Levy* and which *Levy* attempted to distinguish in passing **by implying that it only applied to state taxes.** *California State Bd. of Equalization v. Official Unsecured Creditors Comm. (In re Fidelity Holding Co., Ltd.)*, 837 F.2d 696, 698 (5th Cir. 1988).

There are three commentaries contemporaneous with the period after the 1938 adoption of the Federal Rules of Civil Procedure and the changes to the Bankruptcy Act and the *Erie* decision when the consequences of these three events were being hotly debated: Hill, *The Erie Doctrine in Bankruptcy*, 66 Harv. L. Rev. 1013 (1953) (herein "Hill – Erie"); Hill, *State Procedural Law in Federal Nondiversity Litigation*, 69 Harv. L. Rev. 66 (1955) (herein *"Hill – State"*); and Note, *Tax Claims in Bankruptcy*, 29 Virginia L. Rev. 206 (1942). *Hill – Erie*'s reference to the *Vanston* rationale at page 1017 and at pages 1038 and 1039 states:

> "The theme of the Bankruptcy Act," the Supreme Court has said, "is equality of distribution." But this theme is only barely suggested by the express terms of the Act. The Act does not, as it cannot, say what constitutes equality of distribution; the determination is left to the

> bankruptcy court, as a "court of equity," on a case to case basis. But, in the light of what has been said earlier, the equity power of the bankruptcy court is essentially the power to carry out bankruptcy objectives. . . . It would therefore seem to be a safe working hypothesis that, in pursuance of the bankruptcy objective of equality of distribution, the bankruptcy court is free to apply overriding federal law in determining the consequences of acts of a claimant which created equities in other claimants of a character having relevance only in the context of distribution in insolvency.

Hill – State is a lengthy analysis of the general subject matter involved here and at pages 67, 69, 74, 90, 92 and 97 to 98 has much to say about the general consideration of the issue at bar noting in general that

> in cases where effect is given to state-created substantive rights the courts should be alert to the possible existence of overriding federal policies adopted by Congress in pursuance of a valid legislative object. Thus, however important presumptions may be in the devolution of title to property under state law, the federal tax scheme may shift the burden of proof, for tax purposes, to the taxpayer. And in pursuance of valid bankruptcy objectives Congress may establish presumptions without regard to the presumptions which may arise from the transactions under state law.

As noted in *Vanston*, the court is required to strike an equitable balance between "creditors and creditors" in the distribution process. The district court in the *Levy* case thought that all creditors should be on an equal footing and that the presumption which applied between

a taxpayer and the IRS should not apply between one creditor and another creditor. *In Re Levy*, 130 B.R. 28 (E.D. Va. 1991). Perhaps the validity of that observation is apparent from the analysis of an analogous issue – the applicability to a bankruptcy contested matter of state parole evidence rules and statutes of fraud when the contested matter involves a trustee and the IRS or a state taxing agency.

The parole evidence rule and statutes of frauds are not rules of evidence, rather they are rules of substantive law founded upon the substantive rights of the parties similar for this purpose to burden of proof rules. *Vickery v. Fisher Governor Co.*, 417 F.2d 466, 468 (9th Cir. 1969).

When the parole evidence rule or a statute of frauds is at issue in a bankruptcy proceeding, the bankruptcy court generally must apply the law of the state in which it sits to resolve the issue. *In re Beverly Hills Bancorp*, 649 F.2d 1329, 1334-1335 (9th Cir. 1981); *In re California Pump & Mfg. Co., Inc.*, 588 F.2d 717 (9th Cir. 1978).

Notwithstanding the rule regarding applicability of substantive law, however, it is clear that in a contested matter in bankruptcy court between a trustee and the IRS, the IRS could not assert the rule or the statute as a bar to the admission of evidence. In *Mustard v. U.S.*, 155 F. Supp. 325 (Ct. Cl. 1957) the taxpayer transferred an interest in a promissory note to a charitable beneficiary under a written assignment transferring absolute ownership on the face of the instrument of transfer as compensation for services rendered by the transferee. The IRS disallowed the deduction on the grounds that the transfer was for

services rendered by the trustee as specified in the instrument of transfer. The taxpayer contended that the transfer was subject to an oral trust under which the transferee was to hold the property transferred in trust and apply the payments on the note to purposes specified in the terms of the oral agreement. The taxpayer was allowed to prove the existence of an oral trust contrary to the terms of a written instrument unambiguous on its face because the IRS is not a party who can raise either the parole evidence rule or the statute of frauds as a defense in a tax controversy because it was not a party to the transaction at issue. *Id.* at 332-33.

In keeping with the rationale that a bankruptcy proceeding is a division of a res in the custody of the court and that claimants consent to the rules and authority of the court when they file a claim, Martin, *Consent: The Constitutional Basis for Bankruptcy Judge Authority*, 19 Cal. Bk. J. 1 (1991), it does not seem too far fetched to conclude that rules which may apply when contestants are the taxpayer vs. the government need not apply when the contestants are somebody else. As noted in Hunt, *Tax Claims in Bankruptcy Proceedings*, 14 J. of the National Assoc. of Referees in Bankruptcy 3, 5 & 8 (1939) (cataloged in libraries as the first volumes of the current American Bankruptcy Law Journal):

> It seems to me that when bankruptcy intervenes a new element enters upon the scene, viz., the creditors. . . . Once bankruptcy intervenes, however, the creditors are put in the saddle through their trustee. . . . [I]t is settled that the power of the state officials. . . . to determine and levy taxes must yield to the constitutional power of the federal government to establish what it

> reads as just rules for liquidation in bankruptcy. . . . The bankruptcy act was drafted with the principle that "equality is equity" in mind, but there has been a tendency in recent years for the typical bankruptcy proceeding to resolve itself into a process in which one preferred party after another slices off a portion of the available assets with little or no remaining for distribution to general creditors. This process ought not to be extended beyond the clear requirements and control of the statutes.

It is useful to ascertain from other decisions whether there are any clues to how this issue will be decided by the Supreme Court. Certainly the court has followed a policy of treating the government claimant the same as any other claimant. Thus in *United States v. Ron Pair Enterprises, Inc.*, 109 S.Ct. 1026 (1989), this equality of treatment was to the benefit of the government while in *United States v. Whiting Pools, Inc.*, 103 S. Ct. 2309 (1983) this equality was to the government's detriment. ("We see no reason why a different result should obtain when the IRS is the creditor." *Id.* at 2315.). More recently the decision in *Patterson v. Shumate*, 112 S. Ct. 2242 (1992) was presaged by the Court's decision in *Guidry v. Sheet Metal Workers Nat. Pension Fund*, 110 S:Ct. 680 (1990) in which the Court stated "[u]nderstandably, there may be a natural distaste for the result we reach here. The statute, however, is clear. In addition, as has been noted above, the malefactor often is not the only beneficiary of the pension", *id.* at 688, thus indicating, with important implications here, that one must look to the real parties in interest in a bankruptcy case to determine issues. *Patterson* also emphasized the desirability of uniform treatment

of pension plans unaffected by state law variations. There is an indication in 11 U.S.C. § 346, 728 and 1146 that the same uniformity in state tax claims was intended by Congress.

As noted, the real parties are the creditors and the equitable objectives of the Bankruptcy Code would be best served by adopting what *Grogan* referred to as "a roughly equal allocation of the risk of error between litigants . . . " *Grogan v. Garner,* 111 S. Ct. 654, 659 (1991). As *Grogan* also noted, adoption of this standard would simplify determination of claims because it is well established that the tax claimant has the burden of persuasion as to priority and dischargeability. "Requiring the creditor to establish by a preponderance of the evidence that his claim is not dischargeable reflects a fair balance between these conflicting interests." *Id.*

The only other authorities cited by *Levy* not replied to above are the quotes from the 1973 Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 137, which can be found in Volume 2 of the Appendix to L. King, *Collier on Bankruptcy* (15th ed. 1993). *Levy* states the report recognizes "the need to create a bankruptcy system which obviates criticism based on the ground which involves the different results likely to be obtained in bankruptcy courts and nonbankruptcy courts" 973 F.2d 265, 270 (4th Cir. 1992). The context of the report from which this quotation was taken dealt with the desirability of having bankruptcy judges removed from administration of cases so that they could be more impartial in adversary proceedings and hardly is relevant to the issue in *Levy*. The same report, however, in the

more germane portion of it which deals with "Determination of Tax Liability by the Bankruptcy Courts" states that: "[t]he customary procedures of litigation of tax liabilities, through the Tax Court or by suit for refund, have in large part been abrogated in cases of bankruptcy . . . Ever since the Chandler Act of 1938, it has been required that the government file its claim for *pre-bankruptcy* taxes, whether previously assessed or not, within the same period required of other creditors . . . " H.R. Doc. No. 137 at 292-293. Perhaps more importantly, the Report cites to *Bailey v. Glover*, 88 U.S. (21 Wall) 342, 346 (1875) which stated: "It is obviously one of the purposes of the Bankrupt Law, that there should be a speedy disposition of the bankrupt's assets. This is only second in importance to securing equality of distribution. The Act is filled with provisions for quick and summary disposal of questions arising in the progress of the case, without regard to usual modes of trial. . . . "

REQUEST FOR RELIEF

Debtor requests that the court affirm the district court's affirmance of the bankruptcy court's findings of fact on the grounds that they are not clearly erroneous, affirm the district court's affirmance of the bankruptcy court's conclusions of law as correct, and reverse the district court's reversal of the bankruptcy court's judgment.

STATEMENT OF RELATED CASES

Pursuant to Circuit Rule 28-2.6, counsel certifies that to the best of his knowledge there are no related cases pending at this time in this Court.

Dated: June 27, 1995

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Elmer Dean Martin III

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